

Ch 1

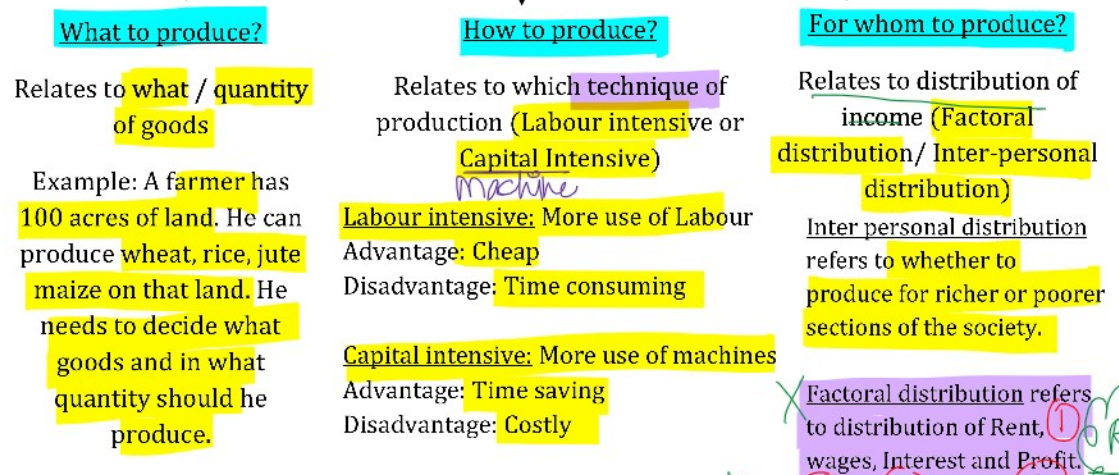
Monday, August 24, 2020 5:57 PM



Types of Economic Problems

→ Central Problems of an Economy / Problem of Resource allocation

Problem of allocation of scarce resources to alternative uses



RWIP

→ Different types of Economy

Market Economy/Capitalist Economy	Centrally Planned Economy/Socialist Economy	Mixed Economy (India)
Producers are free to decide 'what, how and for whom to produce'. It is based on Demand and supply forces in market.	Decisions of 'what, how and for whom to produce' are taken by central authority	Decisions of 'what, how and for whom to produce' are taken on basis of market forces + central authority
The goal is profit maximization.	The goal is to maximize social welfare.	The goal is to have balance between profit maximization and social welfare
Example: USA, <i>other developed economies.</i>	Example: North Korea	Example: India

The price

Government

govt.

producers

① ② ③ ④

→ Production Possibility Curve (PPC)

- ★ PPC is a curve showing possibilities of production of two goods with given resources and technology.
- ★ Also known as Production Possibility Frontier or Transformation Line or Transformation Curve.

Boundary

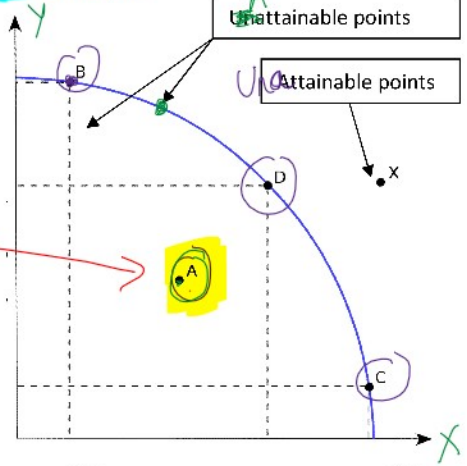
Rough Graph

PPC SCHEDULE → Table

Possibilities	Good X	Good Y	MOC
✓ A	0	100	—
✓ B	10	90	$\frac{10}{10} = 1$
✓ C	20	70	$\frac{20}{10} = 2$
✓ D	30	40	$\frac{30}{10} = 3$
✓ E	40	0	$\frac{40}{10} = 4$

$\frac{\text{Loss}}{\text{Gain}} = \frac{\Delta Y}{\Delta X}$

PPC Graph



- Point A shows underutilization of resources.
- Points B, C and D shows optimum utilization of resources.
- Point X can not be achieved as it is outside PPE.

Assumptions

- Resources are fully utilized
- There is no change in technology
- Only 2 goods are produced

Features

- Slopes downward from left to right
- Concave to the origin

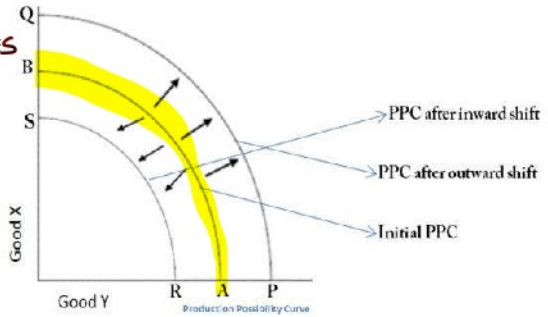
Because if production of one Good is to increase then production of other good has to be sacrificed.

Because of increasing marginal opportunity cost or MRT.



Shifts in PPC

- outward → Rightward shift of PPC indicates increase in resources and/or improvement in technology.
- inward → Leftward shift of PPC indicates decrease in resources and/or degradation in technology.



→ Opportunity Cost refers to the value of next best alternative sacrificed.

★ → Marginal Opportunity Cost (MOC)

- Also known as Marginal Rate of Transformation. (MRT)
- It is defined as the additional units of a good which have to be sacrificed to produce an additional unit of the other good.
- It is expressed as $\Delta Y / \Delta X = \text{Loss of output for an additional unit of Good X.} = \frac{\text{Loss}}{\text{Gain}}$
- It refers to the slope of PPC.

$\Delta = \text{change}$

